

TAX FLASH



Paragraph 20 Underestimation Penalties: Two Levers Worth Revisiting

1. Introduction

The paragraph 20 underestimation penalty is one of the more routinely accepted items on a provisional taxpayer's account. It is levied automatically, reflected quietly in the assessment, and, more often than not, paid without challenge. This flash looks at two levers that deserve more attention than they generally receive.

The first is a set of remittance grounds that the Income Tax Act, No. 58 of 1962 ('the Income Tax Act') itself preserves, and which are, in a specific and often overlooked respect, more favourable than the general remittance grounds in the Tax Administration Act, No. 28 of 2011 ('the TAA'). The second is a procedural argument, grounded in section 214 of the TAA, that where SARS gives notice of the penalty without the particulars that section 214(1) requires, the penalty may not be enforceable against the taxpayer until a compliant notice is given.

The first lever is settled law and simply under-used in practice. The second is a reasonably arguable proposition, properly advanced with its limits acknowledged, on which the only judicial consideration to date, in *ABC (Pty) Ltd v Commissioner for the South African Revenue Services (IT14027) [2016] ZATC 14* ('ABC (Pty) Ltd'), left the point open.

2. How the penalty arises

Paragraph 20(1) of the Fourth Schedule to the Income Tax Act ('the Fourth Schedule') imposes the underestimation penalty where a provisional taxpayer's final or last estimate falls short of actual taxable income by more than a specified margin. Where taxable income exceeds R1 million, the trigger is an estimate below 80% of actual taxable income; where taxable income is R1 million or less, the trigger is an estimate below 90% of actual taxable income and below the applicable 'basic amount'.

Two changes are in the pipeline and should be flagged to clients now. The Draft Tax Administration Laws Amendment Bill, 2026, published for public comment on 29 July 2026, proposes to raise the R1 million threshold in paragraph 20(1) to R1 800 000 with effect from years of assessment commencing on or after 1 March 2026, which is the year currently in progress. The same clause proposes a new proviso, with effect from 25 February 2026, under which the estimate is deemed to be equal to the payment actually made, or nil where no payment was made. The practical consequence of that proviso is significant: a taxpayer who estimates accurately but pays late or short would face the underestimation penalty on the unpaid portion, and not merely the paragraph 27 late-payment penalty. Both remain proposals at the date of writing, and the thresholds and calculation described above are those of the law as it currently stands.

Paragraph 19(6) sets a further trap. If a provisional taxpayer fails to submit an estimate by the last day of the period of four months after the last day of the year of assessment, that taxpayer is deemed, for the purposes of paragraphs 19 and 20, to have submitted an estimate of nil taxable income. A nil estimate, tested against any positive taxable income, all but guarantees that the paragraph 20 threshold is breached. The deeming is, however, expressly subject to paragraph 19(2). Where the Commissioner has himself or herself estimated the taxable income under that subparagraph, there is no deemed nil estimate, and that is worth checking before the penalty is conceded.

The bridge into the TAA is built into paragraph 20(1) itself: the penalty imposed under paragraph 20 is expressly deemed to be a percentage based penalty imposed under Chapter 15 of the TAA. This deeming provision is what draws in section 213, and with it engages Part D (sections 214 and 215) and Part E (sections 216 to 220).

It is worth distinguishing this penalty, in passing, from two others with which it is sometimes conflated: the paragraph 27 late-payment penalty, which is a distinct 10% penalty for late payment rather than underestimation, and the Chapter 16 understatement penalty, which operates under an entirely separate percentage table and behavioural test. The paragraph 27 penalty is nonetheless relevant to quantum. Paragraph 20(2B) requires that any paragraph 20 penalty be reduced by any paragraph 27(1) penalty imposed in respect of the second period payment referred to in paragraph 21(1)(b) or 23(1)(b), and that reduction is easily missed on the face of an assessment.

3. Remittance: The ITA grounds that the TAA preserves

The general architecture of remittance under the TAA sits in Part E of Chapter 15: section 216 (failure to register), section 217 (nominal or first incidence of non-compliance) and section 218 (exceptional circumstances). Section 215 sets out the procedure for making a remittance request under any of these grounds, and section 219 permits SARS, within three years of the penalty assessment, to issue an altered assessment where a penalty was not assessed in accordance with Chapter 15.

Section 217 warrants a closer look than it usually receives. Section 217(1) applies only to a penalty imposed under section 210 or section 212, and so does not reach the paragraph 20 penalty. The applicable provision is section 217(3), which requires that the penalty has been imposed in respect of a 'first incidence' of non-compliance or involves an amount of less than R2 000, that reasonable grounds for the non-compliance exists, and that the non-compliance has been remedied. Those requirements are cumulative. 'First incidence' is itself narrowly defined in section 208 as an incidence of non-compliance where no penalty assessment was issued in the preceding 36 months, whether of the same or a different kind, therefore an unrelated administrative penalty or a paragraph 27 penalty within that window will take the taxpayer outside the section. Section 217(3) is not, however, a dead letter. In *Peri Formwork Scaffolding Engineering (Pty) Ltd v Commissioner for the South African Revenue Service* [2021] ZAWCHC 165; 84 SATC 91, a full bench remitted a 10% late-payment penalty of more than R1 million in its entirety under section 217(3), holding at para [66] that the subsection 'envisages a mechanism to come to the assistance of an aggrieved first incidence non-complying tax payer', and treating the taxpayer's immediate efforts to remedy the default, the absence of prejudice to SARS and the absence of mala fides as reasonable grounds. One caution: at paras [47] and [48] the court described remission of a percentage based penalty as itself limited to R2 000. That reading is hard to reconcile with the wording of section 217(3), in which the R2 000 figure is an

alternative qualifying threshold rather than a cap, and it is contradicted by the court's own order remitting the penalty in full. The point should be anticipated, because SARS can be expected to take it.

The provision that most advisers overlook is section 215(5). It provides that if a tax Act other than the TAA provides remittance grounds for a penalty, SARS may, despite sections 216 to 218, remit the penalty or a portion of it under those other grounds. Paragraph 20 does exactly that.

Paragraph 20(2) allows remittance, in whole or in part, where SARS is satisfied that the estimate was seriously calculated with due regard to the relevant factors and was not deliberately or negligently understated. Paragraph 20(2C) supplies a further, narrower ground: where the paragraph 19(6) deemed nil estimate arose from a failure to submit an estimate, and SARS is satisfied that the failure was not due to an intent to evade or postpone payment of tax, the penalty may be remitted. SARS reads the paragraph 20(2) ground demandingly. Interpretation Note 1 (Issue 3) treats 'seriously calculated' as requiring that the taxpayer have determined the estimate by careful reasoning and judgement using all available information, and states that provisional taxpayers who merely rely on the basic amount are unlikely to meet the requirements for remission.

Hence, a taxpayer who cannot bring itself within section 217(3), whether because the non-compliance is not a first incidence or because the further requirements of that subsection cannot be met, may nonetheless satisfy paragraph 20(2) or paragraph 20(2C) and be remitted via section 215(5).

There is a procedural gate that should not be missed. Section 215(1) requires that the remittance request be made on or before the date for payment stated in the penalty assessment, in the prescribed form and manner, and section 215(2) requires that it describe the circumstances which prevented compliance and be accompanied by the supporting documents and information SARS prescribes.

Section 215(4) allows SARS to extend that period, but it is drawn narrowly. It applies where the non-compliance is an incidence referred to in section 216 or 217 and reasonable grounds exist for the late receipt of the request, or where a circumstance referred to in section 218(2) rendered the person incapable of submitting a timely request. A request resting on the Income Tax Act grounds preserved by section 215(5) does not fit comfortably within either limb, which is a further reason to treat the deadline as a real one. A timeous request does at least buy protection: under section 215(3), no collection steps relating to the penalty may be taken from the day SARS receives the request until 21 business days after notice of its decision, unless SARS has a reasonable belief that

assets are being dissipated or that fraud is involved. The Draft Tax Administration Laws Amendment Bill, 2026 proposes to shorten that period to 10 business days, on a date to be fixed by the Minister.

4. The section 214 question

Section 214(1) provides that a Part B or Part C penalty (which, by the paragraph 20(1) deeming provision, includes the underestimation penalty) is imposed by way of a penalty assessment. Where a penalty assessment is made, SARS must give notice of it to the person, in the format as SARS may decide, including the following particulars: the non-compliance in respect of which the penalty is assessed and its duration; the amount of the penalty imposed; the date for paying the penalty; the automatic increase of the penalty; and a summary of the procedures for requesting remittance of the penalty. The use of the word 'must', read with the word 'including' and the enumerated list which follows, indicates that the above particulars constitute the mandatory content of a valid 'penalty assessment'.

On the basis that the section 214(1) particulars are absent from the notice of assessment, there is a reasonably arguable proposition that no valid penalty assessment has been made and, since section 214(1) provides that the penalty is imposed by way of a penalty assessment, that the penalty may not have been validly imposed, alternatively that it may not be enforceable against the taxpayer.

The fact that the underestimation penalty is reflected together with an assessment for normal tax is not, of itself, objectionable. What section 214(1) nonetheless requires is that the notice of that assessment satisfy the content requirements of section 214(1)(a) to (e).

In the *Nondabula v Commissioner: SARS 2018 (3) SA 541 (ECM)* ('Nondabula') case, the court held that SARS was a creature of statute and acted unlawfully and unconstitutionally when it failed to include the grounds of assessment in the actual notice of assessment, as required by section 96 of the TAA. Although the court did not declare the assessment issued by SARS unlawful, the court granted a prohibitory interdict preventing SARS from taking collection steps in respect of the amount assessed.

Section 214(1) is, for a penalty assessment, the analogue of the provision considered in *Nondabula*: it prescribes, in peremptory terms, the content that the notice must contain. By parity of reasoning, where SARS issues a penalty assessment notice that omits one or more of the particulars required by section 214(1)(a) to (e), SARS acts outside the power conferred by section 214 and contrary to the principle of legality. It follows that SARS should not be entitled to enforce the penalty, and that the penalty falls to be withdrawn.

Furthermore, having regard to the *Singh v Commissioner: SARS 65 SATC 203* case, the court held that a tax debt arises only when a notice of assessment raised by SARS is provided to the taxpayer. Hence, if a notice of assessment is deficient due to not containing the necessary information as prescribed by the relevant section, SARS would not be allowed to enforce payment.

In *ITC1899 79 SATC 315*, it was common cause that a 'penalty assessment' as envisaged in section 214(1) had not been issued. On the court's interpretation, the penalty assessment is the instrument by which the penalty is imposed. Until a penalty assessment complying with section 214 has been issued, an argument can be made that a taxpayer has neither been validly visited with the penalty, nor afforded the opportunity to request its remittance contemplated in section 215.

5. Raising the point in the right place

ABC (Pty) Ltd carries a procedural warning that matters at least as much as the substantive outcome. The taxpayer there lost not because the argument was bad but because it had not been raised in the notice of objection. The governing principle is that stated by Corbett JA in *Matla Coal Ltd v Commissioner for Inland Revenue 1987 (1) SA 108 (A)* at 125C-J, that an appellant is limited on appeal to the grounds stated in its notice of objection. The statutory provision *Matla Coal* construed has since been repealed, but the principle was applied by analogy under the Value-Added Tax Act in *H R Computek (Pty) Ltd v Commissioner, South African Revenue Service [2012] ZASCA 178; 75 SATC 104*, and it is now given effect by rule 32(3) of the Tax Court Rules. On that footing the Tax Court in *ABC (Pty) Ltd* refused the application to amend the grounds of objection, struck out the statement of grounds of appeal and confirmed the penalty. The section 214 argument must therefore appear in the notice of objection from the outset, together with the substantive remittance grounds. It cannot be held back and deployed later before the Tax Board or the Tax Court.

6. Practical takeaways

- On any paragraph 20 penalty reflected in a client's assessment, check whether SARS in fact issued a penalty assessment carrying the section 214(1) particulars, or whether the penalty simply appears on the IT34.
- Check the arithmetic. The penalty is calculated on 80% of actual taxable income, or under paragraph 20(1)(b) on the lesser of 90% of actual taxable income and the basic amount, not on the shortfall, and paragraph 20(2B) requires it to be reduced by any paragraph 27(1) penalty on the second period payment.

- Where the deemed nil estimate in paragraph 19(6) is the trigger, check whether the Commissioner had already estimated the taxable income under paragraph 19(2). If so, the deeming does not apply.
- Watch the Draft Tax Administration Laws Amendment Bill, 2026. The paragraph 20 threshold is proposed to rise to R1 800 000 for years of assessment commencing on or after 1 March 2026, a new proviso would deem the estimate to equal the payment actually made, and the section 215(3) collection hold would fall from 21 to 10 business days.
- Do not stop at the TAA remittance grounds in sections 216 to 218. Paragraph 20(2) and paragraph 20(2C), engaged via section 215(5), may assist where those grounds do not, particularly for a taxpayer who is not a first-time non-complier.
- Mind the section 215(1) timing for any remittance request. Where the penalty is assessed together with the tax, section 214(2)(b) points to the payment date on the tax assessment. The section 215(4) extension is drawn narrowly and does not obviously accommodate a request resting on the

Income Tax Act grounds preserved by section 215(5), so the deadline should be treated as a hard one.

- Where a remittance request is refused, that decision not to remit is itself subject to objection and appeal under Chapter 9, by virtue of section 220.
- The section 214 argument should be advanced as an argument, not asserted as settled law.

7. Conclusion

Two levers deserve more attention than the paragraph 20 penalty usually receives. The first is a settled and under-used set of remittance grounds preserved by the Income Tax Act via section 215(5). The second is a novel, but reasonably arguable, procedural challenge under section 214, resting on the proposition that a penalty of which no compliant notice has been given is not enforceable until one is.

Should you wish to discuss whether either lever applies to a specific assessment, we would be glad to assist.

Disclaimer

The above information is intended to provide general guidance with respect to the subject matter. This general guidance should not be relied on as a basis for undertaking any transaction or business decision, but rather the advice of a qualified tax consultant should be obtained based on a taxpayer's individual circumstances. Although our articles are carefully reviewed, we accept no responsibility in the event of any inaccuracy or omission. For further information please refer to the author.

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